

FINANCIAL STATEMENTS AND REPORT OF
INDEPENDENT CERTIFIED PUBLIC ACCOUNTANTS
SOUTHWEST MEDICAL CENTER
DECEMBER 31, 2014 AND 2013

CONTENTS

	Page
MANAGEMENT'S DISCUSSION AND ANALYSIS	1
REPORT OF INDEPENDENT CERTIFIED PUBLIC ACCOUNTANTS	7
FINANCIAL STATEMENTS	
STATEMENTS OF NET POSITION	9
STATEMENTS OF REVENUES, EXPENSES, AND CHANGES IN NET POSITION	10
STATEMENTS OF CASH FLOWS	11
NOTES TO FINANCIAL STATEMENTS	13
SUPPLEMENTARY INFORMATION	
BALANCE IN DEPOSITORY COMPARED WITH DEPOSITORY SECURITY	28
SCHEDULE OF REVENUES AND EXPENSES WITH BUDGET COMPARISON	29
SUMMARY OF INSURANCE COVERAGE	30

SOUTHWEST MEDICAL CENTER
MANAGEMENT'S DISCUSSION AND ANALYSIS
Years ended December 31, 2014 and 2013

Our discussion and analysis of the financial performance of Southwest Medical Center provides a narrative overview of the Medical Center's financial activities for the years ended December 31, 2014 and 2013. Please read it in conjunction with the accompanying basic financial statements.

Financial highlights

The Medical Center's net position, or equity, increased during each of the past two years, with a \$3,170,263 or 8.5 percent increase during 2014 and a \$2,448,338 or 7.1 percent increase during 2013.

The Medical Center reported a \$763,372 or 26.3 percent increase in operating income for 2014 and a \$1,854,531 or 177.0 percent increase in operating income for 2013.

The net position of Southwest Medical Center Foundation (the Foundation), a component unit of the Medical Center, increased during each of the past two years, with a \$780,536 or 12.8 percent increase during 2014 and a \$561,086 or 10.2 percent increase during 2013.

Using these financial statements

The Medical Center's financial statements consist of three statements - a Statement of Net Position; a Statement of Revenues, Expenses, and Changes in Net Position; and a Statement of Cash Flows. These financial statements and related notes provide information about the activities of the Medical Center, including resources held by or for the benefit of the Medical Center, and resources restricted for specific purposes by contributors, grantors, and indenture agreements.

One of the most important questions asked about the Medical Center's finances is, "Is the Medical Center, as a whole, better or worse off as a result of the year's activities?" The Statement of Net Position and the Statement of Revenues, Expenses, and Changes in Net Position report information about the Medical Center's resources and its activities in a way that helps answer this question. These statements include all restricted and unrestricted assets and all liabilities using the accrual basis of accounting. For purposes of these two statements, revenues and expenses are taken into account regardless of when cash is received or paid.

These two statements report the Medical Center's net position and changes in it. The Medical Center's net position - the difference between assets and liabilities - may be thought of as one way to measure its financial health, or financial position. Over time, increases or decreases in the Medical Center's net position are one indicator of whether its financial health is improving or deteriorating. Consideration must also be given to other nonfinancial indicators, such as changes in the Medical Center's patient base and measures of the quality of service it provides to the community, as well as local economic factors, to assess the overall health of the Medical Center.

The final required statement is the Statement of Cash Flows. The statement reports cash receipts, cash payments, and net changes in cash resulting from operations, investing, and financing activities. It provides answers to such questions as "Where did cash come from?", "What was cash used for?", and "What was the change in cash balance during the reporting period?"

SOUTHWEST MEDICAL CENTER
MANAGEMENT'S DISCUSSION AND ANALYSIS - CONTINUED
Years ended December 31, 2014 and 2013

Assets, liabilities, and net position

The Medical Center's statements of net position as of the end of each of the last three years are summarized as follows:

	<u>2014</u>	<u>2013</u>	<u>2012</u>
Assets			
Current assets	\$ 15,875,551	\$ 13,527,655	\$ 11,928,560
Assets limited as to use	16,722,397	15,302,544	13,381,227
Capital assets, net	<u>27,616,208</u>	<u>28,671,687</u>	<u>30,594,713</u>
Total assets	<u>\$ 60,214,156</u>	<u>\$ 57,501,886</u>	<u>\$ 55,904,500</u>
Liabilities			
Long-term obligations	\$ 16,105,569	\$ 16,325,159	\$ 16,705,379
Current liabilities	<u>3,791,086</u>	<u>4,029,489</u>	<u>4,500,221</u>
Total liabilities	<u>\$ 19,896,655</u>	<u>\$ 20,354,648</u>	<u>\$ 21,205,600</u>
Net position	<u>\$ 40,317,501</u>	<u>\$ 37,147,238</u>	<u>\$ 34,698,900</u>

Cash and cash equivalents in the current asset category increased by \$1,866,194 and \$70,455 during 2014 and 2013, respectively.

Most of the Medical Center's invested cash is set aside by the Board of Trustees for replacement of capital assets or for purchase of additional capital assets. Although, at the discretion of the Board, they may subsequently be used for other purposes, these assets are reported as internally designated assets limited as to use on the statements of net position. This category of assets increased by \$1,418,496 during 2014 and \$2,137,533 during 2013. Net transfers were made from operating cash to this category of assets that totaled \$3,286,494 in 2014 and \$3,076,046 in 2013.

In aggregate, the Medical Center's unrestricted cash and invested cash total was \$17,135,687 and \$13,850,997 as of December 31, 2014 and 2013, respectively. These represent 159 days and 137 days, respectively, of average cash expenses during each of the years then ended. These figures exceed the median values for other hospitals similar to the Medical Center.

The Medical Center's net patient accounts receivable were 55 percent of current assets as of December 31, 2014, 62 percent as of December 31, 2013, and 54 percent as of December 31, 2012. In relation to net patient service revenue, net patient accounts receivable decreased 3.5 percent during 2014, increased 27.8 percent during 2013, and increased 7.6 percent during 2012. The average number of days of net patient revenue represented by them was 72 days, 75 days, and 58 days as of December 31, 2014, 2013, and 2012, respectively. The increase in patient accounts receivable that occurred during 2012 was primarily due to

SOUTHWEST MEDICAL CENTER
MANAGEMENT'S DISCUSSION AND ANALYSIS - CONTINUED
Years ended December 31, 2014 and 2013

employee turnover in the patient financial services department. The increase in patient accounts receivable that occurred during 2013 was primarily due to employee turnover in both the patient financial services department and the clinic billing office.

During 2010, management of the Medical Center determined that expansion and renovation of its patient service area was necessary to meet the current and future health care delivery demands. Management also decided to construct a medical office building for physician clinics located adjacent to and connected with the Medical Center. This endeavor was mostly financed by proceeds from the bonds issued during May 2010 in the amount of \$17,670,000. The medical office building was expected to cost \$4,600,000 and was paid for with available funds of the Medical Center. These two projects were completed and placed into service during 2012. No new long-term obligations were incurred during either 2014 or 2013 other than for a \$295,400 capital lease obligation incurred during 2014.

At the end of 2014, the Medical Center had \$27,616,208 invested in capital assets, net of accumulated depreciation. The total value of new capital assets placed in service totaled \$2,537,409, \$2,459,413, and \$21,053,702 during 2014, 2013, and 2012, respectively.

The Medical Center's net position increased during each of the past three years: \$3,170,263 or 8.5 percent during 2014, \$2,448,338 or 7.1 percent during 2013, and \$1,156,048 or 3.4 percent during 2012. The percentage of total assets financed with its net position, or equity, was 67.0 percent, 64.6 percent, and 62.1 percent as of December 31, 2014, 2013, and 2012, respectively.

The Foundation's statements of net position as of the end of its last three fiscal years ended June 30 are summarized as follows:

	<u>2014</u>	<u>2013</u>	<u>2012</u>
Assets			
Current assets	\$ 6,397,407	\$ 5,538,485	\$ 5,049,519
Capital assets, net	393,063	396,832	400,701
Other investments	<u>70,619</u>	<u>145,236</u>	<u>69,247</u>
Total assets	<u>\$ 6,861,089</u>	<u>\$ 6,080,553</u>	<u>\$ 5,519,467</u>
Liabilities			
Current liabilities	<u>\$ -</u>	<u>\$ -</u>	<u>\$ -</u>
Net position	<u>\$ 6,861,089</u>	<u>\$ 6,080,553</u>	<u>\$ 5,519,467</u>

The Foundation's current assets consist primarily of investments in marketable securities. The Foundation's net position increased \$780,536 or 12.8 percent during fiscal year 2014 and increased \$561,086 or 10.2 percent during fiscal year 2013. These changes in net position were primarily influenced by investment market conditions during those years.

SOUTHWEST MEDICAL CENTER
MANAGEMENT'S DISCUSSION AND ANALYSIS - CONTINUED
Years ended December 31, 2014 and 2013

Operating results and changes in net position

The Medical Center's operating results and changes in net position for each of the last three years are summarized as follows:

	<u>2014</u>	<u>2013</u>	<u>2012</u>
Operating revenues	\$ 45,724,490	\$ 42,157,263	\$ 41,450,206
Operating expenses	<u>42,058,747</u>	<u>39,254,892</u>	<u>40,402,366</u>
Operating income	3,665,743	2,902,371	1,047,840
Interest expense	(718,450)	(705,943)	(281,755)
Nonoperating revenues	47,970	151,910	148,844
Capital grants and contributions	<u>175,000</u>	<u>100,000</u>	<u>241,119</u>
Increase in net position	<u>\$ 3,170,263</u>	<u>\$ 2,448,338</u>	<u>\$ 1,156,048</u>

The first, and most significant, component of the overall change in the Medical Center's net position is its operating income - generally, the difference between net patient service revenue and the expenses incurred to perform those services. Operating income increased \$763,372 during 2014 and increased \$1,854,531 during 2013.

Gross and net patient service revenue for the past three years are analyzed as follows:

	<u>2014</u>	<u>2013</u>	<u>2012</u>
Inpatient services	\$ 46,258,047	\$ 35,274,469	\$ 30,926,853
Outpatient services	65,291,717	60,658,008	57,488,308
Physician services	<u>5,281,779</u>	<u>4,633,195</u>	<u>4,355,946</u>
Gross patient service revenue	116,831,543	100,565,672	92,771,107
Contractual adjustments	(63,081,346)	(51,488,882)	(44,106,178)
Provision for bad debts	(8,295,000)	(6,469,700)	(6,354,780)
Charity care	<u>(1,065,370)</u>	<u>(1,836,329)</u>	<u>(1,658,718)</u>
Net patient service revenue	<u>\$ 44,389,827</u>	<u>\$ 40,770,761</u>	<u>\$ 40,651,431</u>

The Medical Center raised its rates for hospital services by 4.5 percent and 5 percent during January 2014 and January 2015, respectively. The actual changes in gross patient service revenue were different than expected because of changes in patient utilization.

Total inpatient days increased by 14.6 percent and total outpatient registrations decreased by 2.8 percent during 2014. Total inpatient days increased by 3.0 percent and total outpatient registrations decreased by 3.3 percent during 2013.

SOUTHWEST MEDICAL CENTER
MANAGEMENT'S DISCUSSION AND ANALYSIS - CONTINUED
Years ended December 31, 2014 and 2013

In January 2013, the employed orthopedic surgeon left the community. In February and April 2013, two employed general surgeons began active practice for the Medical Center. In May 2013, an employed family practice APRN began practice at the Medical Center. In June 2013, the employed ENT left the community. In October 2013, an internal medicine physician began active practice at the Medical Center. At the end of 2013, the Medical Center had negotiated employment contracts with two hospitalists, and one family practice physician.

In March and November 2014, two employed hospitalists began active practice for the Medical Center. In September 2014, one employed internal physician became a full time hospitalist for the Medical Center. In August 2014, one family practice physician began practice at the Medical Center. In August 2014, one employed internal medicine physician left the community. In August 2014, an employed internal medicine APRN began active practice at the Medical Center.

The Medical Center has agreements with various third-party payors that provide for payments to the Medical Center at amounts different from its established charge rates. These differences are referred to as contractual adjustments. When expressed as a percentage of gross patient service revenue, the Medical Center's contractual adjustments are comparable to median values for similar hospitals.

The Medical Center provides care free of charge or at amounts less than its established rates to patients who meet certain criteria under its charity care policy. Charity care write-offs decreased 42.0 percent during 2014. Charity care write-offs increased 10.7 percent during 2013. The changes during 2014 and 2013 did not occur as a result of policy or criteria changes. The change in 2014 was due to focused efforts by the Medical Center to accurately determine if patients qualified under the charity care policy. There is a continuing trend in the health care industry to identify and report the value of charity care provided to patients.

Together, the provision for bad debts and charity care write-offs represented 8.0 percent, 8.3 percent, and 8.6 percent of gross patient service revenue during 2014, 2013, and 2012, respectively, a relatively stable trend.

Employee salaries and wages increased by \$1,235,126 or 7.3 percent during 2014 and increased by \$85,045 or 0.5 percent during 2013. These changes are functions of changes in numbers of employees and in pay rates. Average pay rates increased by 3.5 percent and 0.8 percent during 2014 and 2013, respectively. Total full-time equivalent employees increased by 12 or 3.7 percent during 2014 after decreasing by 1 or 0.3 percent during 2013. The increase in numbers of employees during 2014 is primarily due to increases in patient volume and efforts to reduce use of contract labor.

The cost of employee benefits was 28.2 percent of salaries and wages during 2014 as compared to 25.0 percent of salaries and wages during 2013. Employee benefit expenses increased \$889,029 during 2014 and decreased \$635,963 during 2013. The primary causes of the changes in both years are variations in costs for workers compensation insurance, public retirement plan contributions, and employee health insurance.

SOUTHWEST MEDICAL CENTER
MANAGEMENT'S DISCUSSION AND ANALYSIS - CONTINUED
Years ended December 31, 2014 and 2013

Supplies and other expenses increased by \$308,127 or 2.1 percent during 2014 and decreased by \$1,348,034 or 8.2 percent during 2013. The 2013 decrease occurred primarily because two additional general surgeons were employed and locum tenens surgeons were no longer required to cover general surgery needs. The 2014 increase occurred primarily because the Medical Center experienced an increase in patient volume. Other than for changes in expenses incurred for locum tenens surgeons, these changes are generally consistent with changes in patient volumes experienced by the Medical Center combined with the general rate of health care inflation.

The Foundation's operating results and changes in net position for each of its last three fiscal years ended June 30 are summarized as follows:

	<u>2014</u>	<u>2013</u>	<u>2012</u>
Contributions	\$ 144,479	\$ 100	\$ 50
Investment income (loss)	799,481	629,255	(17,729)
Other income	109,397	109,225	112,919
Expenses	<u>(272,821)</u>	<u>(177,494)</u>	<u>(324,101)</u>
Change in net position	<u>\$ 780,536</u>	<u>\$ 561,086</u>	<u>\$ (228,861)</u>

Unrealized gains and losses are included in the investment income category on the Foundation's financial statements. The Foundation's investment income included net realized and unrealized losses of \$215,211 during the year ended June 30, 2012, and included net realized and unrealized gains of \$464,271 during the year ended June 30, 2013, and \$637,310 during the year ended June 30, 2014. These results followed changes in the broad market indices during those years.



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REPORT OF INDEPENDENT CERTIFIED PUBLIC ACCOUNTANTS

Board of Trustees
Southwest Medical Center

We have audited the accompanying financial statements of the business-type activity and discretely presented component unit of Southwest Medical Center (the Medical Center) as of and for the years ended December 31, 2014 and 2013, which collectively comprise the Medical Center's basic financial statements as listed in the table of contents, and the related notes to the financial statements.

Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these financial statements in accordance with accounting principles generally accepted in the United States of America; this includes the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error.

Auditor's Responsibility

Our responsibility is to express our opinion on these financial statements based on our audits. We conducted our audits in accordance with auditing standards generally accepted in the United States of America and the Kansas Municipal Audit Guide. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Opinion

In our opinion, the financial statements referred to previously present fairly, in all material respects, the respective financial position of the business-type activity and discretely presented component unit of Southwest Medical Center as of December 31, 2014 and 2013, and the respective changes in financial position and cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America.

Other Matters

Accounting principles generally accepted in the United States of America require that management's discussion and analysis on pages 1 through 6 be presented to supplement the basic financial statements. Such information, although not a part of the basic financial statements, is required by the Governmental Accounting Standards Board, who considers it to be an essential part of financial reporting for placing the financial statements in an appropriate operational, economic, or historical context. We have applied certain limited procedures to the required supplementary information in accordance with auditing standards generally accepted in the United States of America, which consisted of inquiries of management about the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the financial statements, and other knowledge we obtained during our audit of the financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

Our audit was conducted for the purpose of forming opinions on the basic financial statements as a whole. The supplementary information presented on pages 28 through 30 is for purposes of additional analysis and is not a required part of the basic financial statements. Such information is the responsibility of management and was derived from and relates directly to the underlying accounting and other records used to prepare the financial statements. The information has been subjected to the auditing procedures applied in the audit of the financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the financial statements or to the financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, the information is fairly stated in all material respects in relation to the financial statements as a whole, except that no opinion is expressed as to the adequacy of insurance coverage.

Wendling Roe Nelson & Johnson LLC
Topeka, Kansas
March 10, 2015

FINANCIAL STATEMENTS

SOUTHWEST MEDICAL CENTER
STATEMENTS OF NET POSITION
December 31,

	ASSETS			
	2014		2013	
	Medical Center	Component unit	Medical Center	Component unit
CURRENT ASSETS				
Cash and cash equivalents	\$ 3,339,044	\$ 670,667	\$ 1,472,850	\$ 725,803
Marketable securities		5,726,740		4,812,682
Assets limited as to use	447,846		449,057	
Patient accounts receivable, net of allowance for uncollectible accounts of \$6,770,515 in 2014 and \$3,234,354 in 2013	8,765,992		8,342,828	
Estimated third-party payor settlements			90,951	
Other receivables	228,758		264,886	
Inventories	1,457,312		1,356,947	
Prepaid expenses	1,636,599		1,550,136	
Total current assets	<u>15,875,551</u>	<u>6,397,407</u>	<u>13,527,655</u>	<u>5,538,485</u>
ASSETS LIMITED AS TO USE				
Internally designated	13,796,643		12,378,147	
Under indenture agreements - held by trustee	2,862,865		3,008,911	
By contributors and grantors for capital acquisitions	510,735		364,543	
	17,170,243	-	15,751,601	-
Less amounts required to meet current obligations	<u>447,846</u>		<u>449,057</u>	
	<u>16,722,397</u>	-	<u>15,302,544</u>	-
CAPITAL ASSETS - NET	<u>27,616,208</u>	<u>393,063</u>	<u>28,671,687</u>	<u>396,832</u>
OTHER ASSETS				
Other investments		70,619		145,236
Total other assets	-	<u>70,619</u>	-	<u>145,236</u>
Total assets	<u>\$60,214,156</u>	<u>\$ 6,861,089</u>	<u>\$57,501,886</u>	<u>\$ 6,080,553</u>

The accompanying notes are an integral part of these statements.

LIABILITIES AND NET POSITION

	2014		2013	
	Medical Center	Component unit	Medical Center	Component unit
CURRENT LIABILITIES				
Current maturities of long-term obligations	\$ 407,195	\$ -	\$ 355,000	\$ -
Accounts payable	834,312		1,639,554	
Estimated third-party payor settlements	443,454		27,454	
Other accrued liabilities	87,445		205,771	
Accrued salaries and benefits	966,575		829,531	
Accrued compensated absences	754,275		671,050	
Accrued interest payable	297,830		301,129	
Total current liabilities	3,791,086	-	4,029,489	-
LONG-TERM OBLIGATIONS, less current maturities				
	16,105,569		16,325,159	
Total liabilities	19,896,655	-	20,354,648	-
NET POSITION				
Invested in capital assets - net of related debt	11,556,434	393,063	12,547,830	396,832
Restricted				
For debt service	1,570,590		1,624,019	
Expendable for capital acquisitions	1,350,019		1,193,133	
For specific operating activities		575,186		441,198
Nonexpendable permanent endowments		657,779		512,210
Unrestricted	25,840,458	5,235,061	21,782,256	4,730,313
Total net position	40,317,501	6,861,089	37,147,238	6,080,553
Total liabilities and net position	\$60,214,156	\$ 6,861,089	\$57,501,886	\$ 6,080,553

SOUTHWEST MEDICAL CENTER
STATEMENTS OF REVENUES, EXPENSES,
AND CHANGES IN NET POSITION
Year ended December 31,

	2014		2013	
	Medical Center	Component unit	Medical Center	Component unit
Operating revenues				
Net patient service revenue	\$44,389,827	\$ -	\$40,770,761	\$ -
Electronic health record incentives	1,027,210		1,103,469	
Other	307,453		283,033	
Total operating revenues	45,724,490	-	42,157,263	-
Operating expenses				
Salaries and wages	18,138,333		16,903,207	
Employee benefits	5,113,879		4,224,850	
Supplies and other	15,316,318	269,052	15,008,191	173,625
Depreciation and amortization	3,490,217	3,769	3,118,644	3,869
Total operating expenses	42,058,747	272,821	39,254,892	177,494
Operating income (loss)	3,665,743	(272,821)	2,902,371	(177,494)
Nonoperating revenues (expenses)				
Investment income	37,808	799,481	96,619	629,255
Interest expense	(718,450)		(705,943)	
Noncapital grants and contributions	10,162	144,479	55,291	100
Other		109,397		109,225
Total nonoperating revenues (expenses)	(670,480)	1,053,357	(554,033)	738,580
Excess of revenues over expenses before capital grants and contributions	2,995,263	780,536	2,348,338	561,086
Capital grants and contributions	175,000		100,000	
Change in net position	3,170,263	780,536	2,448,338	561,086
Net position at beginning of year	37,147,238	6,080,553	34,698,900	5,519,467
Net position at end of year	\$40,317,501	\$ 6,861,089	\$37,147,238	\$ 6,080,553

The accompanying notes are an integral part of these statements.

SOUTHWEST MEDICAL CENTER
STATEMENTS OF CASH FLOWS
Year ended December 31,

	2014		2013	
	<u>Medical Center</u>	<u>Component unit</u>	<u>Medical Center</u>	<u>Component unit</u>
Cash flows from operating activities				
Receipts from and on behalf of patients	\$44,473,614	\$ -	\$39,141,090	\$ -
Payments to or on behalf of employees	(22,949,095)		(21,304,753)	
Payments for supplies and services	(16,618,785)	(269,052)	(15,515,508)	(173,625)
Other receipts and payments	<u>1,370,791</u>		<u>1,575,908</u>	
Net cash provided (used) by operating activities	<u>6,276,525</u>	<u>(269,052)</u>	<u>3,896,737</u>	<u>(173,625)</u>
Cash flows from noncapital financing activities				
Noncapital grants and contributions	<u>10,162</u>	<u>144,479</u>	<u>55,291</u>	<u>100</u>
Cash flows from capital and related financing activities				
Acquisition of capital assets	(2,325,515)		(1,378,442)	
Capital lease obligation incurred	295,400			
Principal payments on long-term obligations	(437,965)		(180,000)	
Interest paid	(746,579)		(732,650)	
Capital grants and contributions	<u>175,000</u>		<u>100,000</u>	
Net cash used by capital and related financing activities	<u>(3,039,659)</u>	<u>-</u>	<u>(2,191,092)</u>	<u>-</u>
Cash flows from investing activities				
Change in assets limited as to use	(1,431,814)		(1,788,754)	
Change in investments		(276,748)		90,960
Other income received		184,014		33,236
Investment income received	<u>50,980</u>	<u>162,171</u>	<u>98,273</u>	<u>164,984</u>
Net cash provided (used) by investing activities	<u>(1,380,834)</u>	<u>69,437</u>	<u>(1,690,481)</u>	<u>289,180</u>
Net change in cash and cash equivalents	1,866,194	(55,136)	70,455	115,655
Cash and cash equivalents at beginning of year	<u>1,472,850</u>	<u>725,803</u>	<u>1,402,395</u>	<u>610,148</u>
Cash and cash equivalents at end of year	<u>\$ 3,339,044</u>	<u>\$ 670,667</u>	<u>\$ 1,472,850</u>	<u>\$ 725,803</u>

The accompanying notes are an integral part of these statements.

SOUTHWEST MEDICAL CENTER
STATEMENTS OF CASH FLOWS - CONTINUED
Year ended December 31,

	2014		2013	
	<u>Medical Center</u>	<u>Component unit</u>	<u>Medical Center</u>	<u>Component unit</u>
Reconciliation of operating income (loss) to net cash provided (used) by operating activities				
Operating income (loss)	\$ 3,665,743	\$ (272,821)	\$ 2,902,371	\$ (177,494)
Adjustments to reconcile operating income (loss) to net cash provided (used) by operating activities				
Depreciation and amortization	3,490,217	3,769	3,118,644	3,869
Provision for bad debts	8,295,000		6,469,700	
Changes in				
Accounts receivable	(8,718,164)		(8,321,397)	
Other receivables	36,128		189,406	
Inventories and prepaid expenses	(186,828)		(389,180)	
Accounts payable and accrued expenses	(812,522)		(294,833)	
Estimated third-party payor settlements	<u>506,951</u>	<u></u>	<u>222,026</u>	<u></u>
Net cash provided (used) by operating activities	<u>\$ 6,276,525</u>	<u>\$ (269,052)</u>	<u>\$ 3,896,737</u>	<u>\$ (173,625)</u>

The accompanying notes are an integral part of these statements.

SOUTHWEST MEDICAL CENTER
NOTES TO FINANCIAL STATEMENTS
December 31, 2014 and 2013

NOTE A - DESCRIPTION OF REPORTING ENTITY AND SUMMARY OF SIGNIFICANT
ACCOUNTING POLICIES

1. Reporting entity

Southwest Medical Center (the Medical Center) is located in Liberal, Kansas, and is owned by Seward County, Kansas (the County), and governed by a seven-member Board of Trustees appointed by the Board of County Commissioners of the County. The Medical Center is a 101-bed, not-for-profit general hospital. The Medical Center can sue and be sued, and can buy, sell, or lease real property. Bond issuances must be approved by the County. The Medical Center is a component unit of the County.

The component unit discussed in Note A2 is included in the Medical Center's reporting entity because of the nature and significance of its relationship with the Medical Center.

2. Component unit

The financial statements include the financial data of the discretely presented component unit described below. The component unit is reported separately to emphasize that it is legally separate from the Medical Center.

Southwest Medical Center Foundation, Inc. (the Foundation), is a not-for-profit corporation formed in August of 1980 to receive, invest, and disburse funds received for the benefit, support, and maintenance of the Medical Center. The Foundation is administered by a Board of Trustees. Three of the seven members of that Board are also members of the Medical Center's Board of Trustees.

Financial data of the Foundation are presented as of June 30, 2014 and 2013, and for the years then ended.

3. Use of estimates

The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from these estimates.

4. Basis of accounting

The Medical Center uses enterprise fund accounting. Revenues and expenses are recognized on the accrual basis using the economic resources measurement focus.

5. Cash and cash equivalents

The Medical Center considers all cash and invested cash to be cash equivalents, excluding any assets limited as to use and items classified as investments by the Foundation.

SOUTHWEST MEDICAL CENTER
NOTES TO FINANCIAL STATEMENTS - CONTINUED
December 31, 2014 and 2013

NOTE A - DESCRIPTION OF REPORTING ENTITY AND SUMMARY OF SIGNIFICANT
ACCOUNTING POLICIES - Continued

6. Allowance for uncollectible accounts

The Medical Center provides for accounts receivable that could become uncollectible in the future by establishing an allowance to reduce the carrying value of such receivables to their estimated net realizable value. The Medical Center estimates this allowance based on the aging of its accounts receivable and its historical collection experience for each type of payor.

7. Inventories

Inventories are stated at the lower of cost or market with cost determined on the first-in, first-out method.

8. Investments and investment income

Investments in debt and equity securities are reported at fair value. Interest, dividends, and gains and losses, both realized and unrealized, on investments in debt and equity securities are included in nonoperating revenue when earned.

9. Assets limited as to use

Assets limited as to use include assets set aside by the Board of Trustees for replacement of capital assets or for purchase of additional capital assets, over which the Board retains control and may at its discretion subsequently use for other purposes; assets held by a trustee under indenture agreements; and assets restricted by contributors and grantors for capital acquisitions. Assets limited as to use that are required for obligations classified as current liabilities are reported in current assets.

10. Capital assets

Capital assets (including assets recorded as capital leases) are stated at cost. Depreciation and amortization of capital assets are provided on the straight-line method over the estimated useful lives of the assets. The estimated lives used are generally in accordance with the guidelines established by the American Hospital Association.

The costs of maintenance and repairs are charged to operating expenses as incurred. The costs of significant additions, renewals, and betterments to depreciable properties are capitalized and depreciated over the remaining or extended estimated useful lives of the item or the properties. Gains and losses on disposition of capital assets are included in nonoperating revenues and expenses.

11. Costs of borrowing

Interest costs (including amortization of bond premium) incurred on borrowed funds during the period of construction of capital assets are capitalized as a component of the cost of acquiring those assets. Original issue premiums and discounts associated with issuance of long-term debt are amortized using the interest method over the term of the related debt.

SOUTHWEST MEDICAL CENTER
NOTES TO FINANCIAL STATEMENTS - CONTINUED
December 31, 2014 and 2013

NOTE A - DESCRIPTION OF REPORTING ENTITY AND SUMMARY OF SIGNIFICANT
ACCOUNTING POLICIES - Continued

12. Grants and contributions

From time to time, the Medical Center receives grants and contributions from individuals and private organizations. Revenues from grants and contributions are recognized when all eligibility requirements, including time requirements, are met. Grants and contributions may be restricted for specific operating purposes or for capital purposes. Amounts that are unrestricted or that are restricted to a specific operating purpose are reported as nonoperating revenues. Amounts restricted to capital acquisitions are reported after nonoperating revenues and expenses.

13. Estimated health insurance claims payable

The Medical Center is self-insured for health insurance claims of its employees. Management estimates the net liability for reported and unreported claims incurred as of the end of each reporting period. These estimates are based on known claims and historical claims experience.

Management believes that estimates for health insurance claims payable are reasonable. However, it is possible that actual incurred claims expense may vary significantly from the estimate included in the accompanying financial statements.

14. Net position

The net position of the Medical Center is classified into four components. "Net position invested in capital assets net of related debt" consists of capital assets net of accumulated depreciation reduced by the balances of any outstanding borrowings used to finance the purchase or construction of those assets. "Restricted expendable net position" is the noncapital net position that must be used for a particular purpose, as specified by creditors, grantors, or contributors external to the Medical Center, including amounts deposited with trustees as required by indenture agreements. "Restricted nonexpendable net position" equals the principal portion of permanent endowments. "Unrestricted net position" is the remaining net position that does not meet the definitions of the other three components of net position.

15. Operating revenues and expenses

The Medical Center's statement of revenues, expenses, and changes in net position distinguishes between operating and nonoperating revenues and expenses. Operating revenues result from exchange transactions associated with providing health care services, which is the Medical Center's principal activity. Nonexchange revenues, including noncapital grants and contributions, are reported as nonoperating revenues. Operating expenses are all expenses incurred to provide health care services, other than financing costs.

SOUTHWEST MEDICAL CENTER
NOTES TO FINANCIAL STATEMENTS - CONTINUED
December 31, 2014 and 2013

NOTE A - DESCRIPTION OF REPORTING ENTITY AND SUMMARY OF SIGNIFICANT
ACCOUNTING POLICIES - Continued

16. Net patient service revenue

Net patient service revenue is reported at established charges with deductions for discounts, charity care, contractual adjustments, and provision for bad debts, including estimated retroactive adjustments under reimbursement agreements with third-party payors. Retroactive adjustments are accrued on an estimated basis in the period the related services are rendered and adjusted in future periods as final settlements are determined.

17. Charity care

The Medical Center provides care to patients who meet certain criteria under its charity care policy without charge or at amounts less than its established rates. Because the Medical Center does not pursue collection of amounts determined to qualify as charity care, they are not reported as revenue.

18. Income taxes

The Medical Center is exempt from federal income taxes pursuant to Sections 115 and 501(a) of the Internal Revenue Code. Management is not aware of any uncertainties in income tax positions. Tax years ending on and before December 31, 2010, are not subject to examination by taxing authorities.

The Foundation is a not-for-profit corporation as described in Section 501(c)(3) of the Internal Revenue Code and is exempt from federal income taxes on its related income pursuant to Section 501(a) of the Code. Management is not aware of any uncertainties in income tax positions. Tax years ending on and before June 30, 2010, are not subject to examination by taxing authorities.

19. Subsequent events

The Medical Center has evaluated subsequent events through March 10, 2015, which is the date the financial statements were available to be issued.

NOTE B - REIMBURSEMENT PROGRAMS

The Medical Center has agreements with third-party payors that provide for payments to the Medical Center at amounts different from its established charge rates. The amounts reported on the balance sheets as estimated third-party payor settlements consist of the estimated differences between the contractual amounts for providing covered services and the interim payments received for those services. A summary of the payment arrangements with major third-party payors follows:

Medicare - Inpatient acute care services rendered to Medicare program beneficiaries are paid at prospectively determined rates per discharge. Inpatient skilled nursing services are paid at prospectively determined per diem rates. Outpatient services are paid at prospectively determined rates per occasion of service. Physician services rendered to Medicare beneficiaries are paid based on a prospectively determined fee schedule.

SOUTHWEST MEDICAL CENTER
NOTES TO FINANCIAL STATEMENTS - CONTINUED
December 31, 2014 and 2013

NOTE B - REIMBURSEMENT PROGRAMS - Continued

Prospectively determined rates vary according to patient classification systems that are based on clinical, diagnostic, and other factors. The Medical Center is paid for cost reimbursable and other items at tentative rates with final settlement determined after submission of annual cost reports by the Medical Center and audits or reviews thereof by the Medicare administrative contractor. The Medical Center's classification of patients under the Medicare program and the appropriateness of their admission are subject to an independent review by a peer review organization. The Medical Center's Medicare cost reports have been audited or reviewed by the Medicare administrative contractor through December 31, 2011.

Medicaid - Inpatient acute care services rendered to Medicaid program beneficiaries are paid at prospectively determined rates per discharge. These rates vary according to a patient classification system that is based on clinical, diagnostic, and other factors. All other services rendered to Medicaid beneficiaries are paid at prospective rates determined on either a per diem or a fee-for-service basis.

Blue Cross and Blue Shield - All services rendered to patients who are insured by Blue Cross and Blue Shield are paid on the basis of prospectively determined rates per discharge or discounts from established charges.

The Medical Center has also entered into payment agreements with certain commercial insurance carriers and preferred provider organizations. The basis for payment to the Medical Center under these agreements includes prospectively determined rates per discharge, discounts from established charges, and prospectively determined daily rates.

A summary of gross and net patient service revenue follows:

	<u>2014</u>	<u>2013</u>
Gross patient service revenue	\$ 116,831,543	\$ 100,565,672
Contractual adjustments	(63,081,346)	(51,488,882)
Provision for bad debts	(8,295,000)	(6,469,700)
Charity care	<u>(1,065,370)</u>	<u>(1,836,329)</u>
Net patient service revenue	<u>\$ 44,389,827</u>	<u>\$ 40,770,761</u>

Revenue from the Medicare and Medicaid programs accounted for approximately 24 percent and 11 percent, respectively, of the Medical Center's net patient service revenue during 2014, and 21 percent and 13 percent, respectively, of the Medical Center's net patient service revenue during 2013. Laws and regulations governing the Medicare and Medicaid programs are extremely complex and subject to interpretation. As a result, there is at least a reasonable possibility that recorded estimates will change by a material amount in the near term.

SOUTHWEST MEDICAL CENTER
NOTES TO FINANCIAL STATEMENTS - CONTINUED
December 31, 2014 and 2013

NOTE C - ELECTRONIC HEALTH RECORD INCENTIVE PAYMENTS

The American Recovery and Reinvestment Act of 2009 (ARRA) provides for incentive payments under the Medicare and Medicaid programs for certain hospitals and physician practices that demonstrate meaningful use of certified electronic health record (EHR) technology. These provisions of ARRA are intended to promote the adoption and meaningful use of interoperable health information technology and qualified EHR technology.

The Medical Center recognizes revenue for EHR incentive payments when it has reasonable assurance that it has demonstrated meaningful use of certified EHR technology for the applicable period and complied with the reporting conditions to receive the payment. The demonstration of meaningful use is based upon meeting a series of objectives and varies between hospital facilities and physician practices and between the Medicare and Medicaid programs. Additionally, meeting the objectives in order to demonstrate meaningful use becomes progressively more stringent as its implementation is phased in through stages as outlined by CMS. During the years ended December 31, 2014 and 2013, the Medical Center recognized \$1,027,210 and \$1,103,469, respectively, of revenue for EHR incentive payments.

The Medical Center incurs both capital expenditures and operating expenses in connection with the implementation of its EHR initiatives. The amounts and timing of these expenditures do not directly correlate with the timing of the Medical Center's recognition of EHR incentive payments as revenue.

NOTE D - DEPOSITS WITH FINANCIAL INSTITUTIONS

Kansas statutes authorize the Medical Center, with certain restrictions, to deposit or invest in open accounts, time deposits, certificates of deposit, repurchase agreements, U.S. Treasury Bills and Notes, and the State Treasurer's investment pool. Kansas statutes also require that collateral be pledged for bank deposits with a fair market value equal to 100 percent of the uninsured amounts and must be assigned for the benefit of the Medical Center.

At December 31, 2014, the carrying amount of the Medical Center's bank deposits, including certificates of deposit, was \$17,638,164 and the bank balances were \$18,527,500. Of the bank balances, \$500,000 was covered by federal depository insurance and \$18,027,500 was covered by collateral held by a third-party bank, but not registered in the Medical Center's name.

SOUTHWEST MEDICAL CENTER
NOTES TO FINANCIAL STATEMENTS - CONTINUED
December 31, 2014 and 2013

NOTE D - DEPOSITS WITH FINANCIAL INSTITUTIONS - Continued

The Medical Center's bank deposits are included in the financial statements under the following categories:

Cash and cash equivalents	\$ 3,335,970
Assets limited as to use	
Internally designated	13,791,459
By contributors and grantors for capital acquisitions	<u>510,735</u>
Total bank deposits	<u>\$ 17,638,164</u>

NOTE E - INVESTMENTS

The Foundation's investments are stated at fair value. The composition of its investments is as follows:

	<u>2014</u>	<u>2013</u>
Equity securities	\$ 5,586,019	\$ 4,524,866
Fixed income securities	<u>140,721</u>	<u>287,816</u>
	<u>\$ 5,726,740</u>	<u>\$ 4,812,682</u>

NOTE F - ASSETS LIMITED AS TO USE

The composition of assets limited as to use is as follows:

	<u>2014</u>	<u>2013</u>
Internally designated		
Cash	\$ 6,291,459	\$ 4,876,191
Certificates of deposit	7,500,000	7,500,000
Accrued interest receivable	<u>5,184</u>	<u>1,956</u>
	<u>\$ 13,796,643</u>	<u>\$ 12,378,147</u>
Under indenture agreements - held by trustee		
U.S. Treasury obligations	\$ 2,862,865	\$ 2,992,511
Accrued interest receivable	<u> </u>	<u>16,400</u>
	<u>\$ 2,862,865</u>	<u>\$ 3,008,911</u>
By contributors and grantors for capital acquisitions		
Cash	<u>\$ 510,735</u>	<u>\$ 364,543</u>

SOUTHWEST MEDICAL CENTER
NOTES TO FINANCIAL STATEMENTS - CONTINUED
December 31, 2014 and 2013

NOTE G - CAPITAL ASSETS

Capital asset additions, retirements, and balances for the Medical Center are as follows:

	2014			
	<u>Beginning balance</u>	<u>Transfers and additions</u>	<u>Retirements</u>	<u>Ending balance</u>
Land	\$ 104,046	\$ -	\$ -	\$ 104,046
Land improvements	2,951,334			2,951,334
Buildings and fixed equipment	41,104,356	122,943		41,227,299
Major movable equipment	35,171,616	2,414,466		37,586,082
Totals at historical cost	<u>79,331,352</u>	<u>2,537,409</u>	<u>-</u>	<u>81,868,761</u>
Less accumulated depreciation and amortization				
Land improvements	989,929	106,732		1,096,661
Buildings and fixed equipment	22,399,702	1,286,571		23,686,273
Major movable equipment	28,674,385	2,096,914		30,771,299
	<u>52,064,016</u>	<u>3,490,217</u>	<u>-</u>	<u>55,554,233</u>
	27,267,336	(952,808)	-	26,314,528
Construction in progress	<u>1,404,351</u>	<u>(102,671)</u>		<u>1,301,680</u>
Capital assets, net	<u>\$28,671,687</u>	<u>\$ (1,055,479)</u>	<u>\$ -</u>	<u>\$27,616,208</u>

	2013			
	<u>Beginning balance</u>	<u>Transfers and additions</u>	<u>Retirements</u>	<u>Ending balance</u>
Land	\$ 104,046	\$ -	\$ -	\$ 104,046
Land improvements	2,165,744	785,590		2,951,334
Buildings and fixed equipment	41,623,326	(518,970)		41,104,356
Major movable equipment	32,978,823	2,192,793		35,171,616
Totals at historical cost	<u>76,871,939</u>	<u>2,459,413</u>	<u>-</u>	<u>79,331,352</u>
Less accumulated depreciation and amortization				
Land improvements	883,197	106,732		989,929
Buildings and fixed equipment	21,047,842	1,351,860		22,399,702
Major movable equipment	27,014,333	1,660,052		28,674,385
	<u>48,945,372</u>	<u>3,118,644</u>	<u>-</u>	<u>52,064,016</u>
	27,926,567	(659,231)	-	27,267,336
Construction in progress	<u>2,668,146</u>	<u>(1,263,795)</u>		<u>1,404,351</u>
Capital assets, net	<u>\$30,594,713</u>	<u>\$ (1,923,026)</u>	<u>\$ -</u>	<u>\$28,671,687</u>

SOUTHWEST MEDICAL CENTER
NOTES TO FINANCIAL STATEMENTS - CONTINUED
December 31, 2014 and 2013

NOTE G - CAPITAL ASSETS - Continued

Construction in progress at December 31, 2014 and 2013, consisted mainly of costs incurred for various items of equipment, software upgrades, and planning costs for building renovation projects. A summary of outstanding contract commitments for the building renovation projects as of December 31, 2014, is as follows:

Total commitment	\$ 3,289,090
Costs incurred to date	<u>(190,130)</u>
Remaining commitment	<u>\$ 3,098,960</u>

Capital asset additions, retirements, and balances for the Foundation are as follows:

	2014			
	<u>Beginning balance</u>	<u>Transfers and additions</u>	<u>Retirements</u>	<u>Ending balance</u>
Land	\$ 374,526	\$ -	\$ -	\$ 374,526
Land improvements	96,231			96,231
Major movable equipment	<u>2,079</u>			<u>2,079</u>
Totals at historical cost	472,836	-	-	472,836
Less accumulated depreciation and amortization	<u>76,004</u>	<u>3,769</u>		<u>79,773</u>
Capital assets, net	<u>\$ 396,832</u>	<u>\$ (3,769)</u>	<u>\$ -</u>	<u>\$ 393,063</u>

	2013			
	<u>Beginning balance</u>	<u>Transfers and additions</u>	<u>Retirements</u>	<u>Ending balance</u>
Land	\$ 374,526	\$ -	\$ -	\$ 374,526
Land improvements	96,231			96,231
Major movable equipment	<u>2,079</u>			<u>2,079</u>
Totals at historical cost	472,836	-	-	472,836
Less accumulated depreciation and amortization	<u>72,135</u>	<u>3,869</u>		<u>76,004</u>
Capital assets, net	<u>\$ 400,701</u>	<u>\$ (3,869)</u>	<u>\$ -</u>	<u>\$ 396,832</u>

SOUTHWEST MEDICAL CENTER
NOTES TO FINANCIAL STATEMENTS - CONTINUED
December 31, 2014 and 2013

NOTE H - LONG-TERM OBLIGATIONS

Long-term obligations are summarized as follows:

	<u>2014</u>	<u>2013</u>
2.0% to 5.0% General Obligation Hospital Refunding and Improvement Bonds, Series 2010-A; issued on May 27, 2010, in the original amount of \$17,670,000, due serially through August 1, 2040, including unamortized premium of \$380,329 in 2014 and \$405,159 in 2013	\$ 16,300,329	\$ 16,680,159
Capital lease obligation, imputed interest rate of 7.4%, collateralized by leased equipment with an amortized cost of \$205,139 at December 31, 2014	<u>212,435</u>	<u> </u>
	16,512,764	16,680,159
Less current maturities	<u>407,195</u>	<u>355,000</u>
	<u>\$ 16,105,569</u>	<u>\$ 16,325,159</u>

On May 27, 2010, the County issued \$17,670,000 in General Obligation Hospital Refunding and Improvement Bonds, Series 2010-A, (the 2010-A bonds) on behalf of the Medical Center pursuant to a bond trust indenture dated May 1, 2010. The proceeds of the bonds were used, together with other available funds of the Medical Center, for the purpose of providing funds to (1) expand and renovate the Medical Center's existing facilities, (2) pay for the costs of certain items of equipment, (3) fund a debt service reserve fund, (4) pay certain costs related to issuance of the bonds, and (5) make the payment as scheduled on August 1, 2010, for principal and interest due then on the 2001-A bonds.

The indenture agreements for the bonds require the Medical Center to transfer to a trustee, on a monthly basis, specified amounts which, when combined with interest earned on the respective funds held by the trustee, will provide sufficient funds to pay the bond principal and interest on the appropriate due dates. Such amounts were maintained and are included with assets limited as to use in the financial statements. The indenture agreements also include certain restrictive covenants relating to the acquisition and disposition of property, incurrence of additional indebtedness, and level of fees and rates charged.

SOUTHWEST MEDICAL CENTER
NOTES TO FINANCIAL STATEMENTS - CONTINUED
December 31, 2014 and 2013

NOTE H - LONG-TERM OBLIGATIONS - Continued

Scheduled annual debt service requirements on long-term debt are as follows:

	<u>Principal</u>	<u>Interest</u>	<u>Total</u>
2015	\$ 360,000	\$ 721,062	\$ 1,081,062
2016	370,000	712,062	1,082,062
2017	380,000	700,963	1,080,963
2018	395,000	688,613	1,083,613
2019	410,000	675,775	1,085,775
2020 - 2024	2,255,000	3,155,715	5,410,715
2025 - 2029	2,745,000	2,670,250	5,415,250
2030 - 2034	3,505,000	1,917,750	5,422,750
2035 - 2039	4,470,000	949,750	5,419,750
2040	<u>1,030,000</u>	<u>51,500</u>	<u>1,081,500</u>
	<u>\$ 15,920,000</u>	<u>\$ 12,243,440</u>	<u>\$ 28,163,440</u>

The following is a yearly schedule of future minimum lease payments under capital lease obligations as of December 31, 2014:

	<u>Principal</u>	<u>Interest</u>	<u>Total</u>
2015	\$ 47,195	\$ 14,165	\$ 61,360
2016	50,782	10,578	61,360
2017	54,715	6,645	61,360
2018	55,005	2,566	57,571
2019	<u>4,738</u>	<u>30</u>	<u>4,768</u>
	<u>\$ 212,435</u>	<u>\$ 33,984</u>	<u>\$ 246,419</u>

The following is a summary of changes in long-term obligations:

	<u>Capital lease obligation</u>	<u>Bonds</u>	<u>Total long-term obligations</u>
Outstanding at January 1, 2013	\$ -	\$ 16,885,379	\$ 16,885,379
Principal payments		(180,000)	(180,000)
Amortization of premium		<u>(25,220)</u>	<u>(25,220)</u>
Outstanding at January 1, 2014	-	16,680,159	16,680,159
Obligations incurred	295,400		295,400
Principal payments	(82,965)	(355,000)	(437,965)
Amortization of premium		<u>(24,830)</u>	<u>(24,830)</u>
Outstanding at December 31, 2014	<u>\$ 212,435</u>	<u>\$ 16,300,329</u>	<u>\$ 16,512,764</u>

SOUTHWEST MEDICAL CENTER
NOTES TO FINANCIAL STATEMENTS - CONTINUED
December 31, 2014 and 2013

NOTE H - LONG-TERM OBLIGATIONS - Continued

Total interest costs are summarized as follows:

	<u>2014</u>	<u>2013</u>
Total interest incurred	\$ 743,280	\$ 731,163
Amortization of bond premium	<u>(24,830)</u>	<u>(25,220)</u>
Interest expense	<u>\$ 718,450</u>	<u>\$ 705,943</u>

NOTE I - DEFINED BENEFIT PENSION PLAN

The Medical Center participates in the Kansas Public Employees Retirement System (KPERS), a cost-sharing multiple-employer defined benefit pension plan as provided by K.S.A. 74-4901, et. seq. Substantially all employees of the Medical Center are eligible to participate in KPERS following the completion of one year of service. KPERS provides retirement benefits, life insurance, disability income benefits, and death benefits. Kansas law establishes and amends benefit provisions. KPERS issues a publicly available financial report that includes financial statements and required supplementary information. That report may be obtained by writing to KPERS (611 S. Kansas Avenue, Topeka, Kansas 66603-3803) or by calling 1-888-275-5737.

K.S.A. 74-4919 establishes the KPERS member-employee contribution rate at 4 percent of covered salary for employees hired prior to July 1, 2009, and 6 percent of covered salary for employees hired on or after July 1, 2009. The employer collects and remits member-employee contributions according to the provisions of Section 414(h) of the Internal Revenue Code. State law provides that the employer contribution rate be determined annually based on the results of an annual actuarial valuation.

KPERS is funded on an actuarial reserve basis. State law sets a limitation on annual increases in the contribution rates for KPERS employers. The employer rates established by statute for calendar years 2014 and 2013 were 9.69 percent and 8.62 percent, respectively. The Medical Center's employer contributions to KPERS for the years ended December 31, 2014 and 2013, were \$1,601,436 and \$1,395,666, respectively, equal to the statutory required contributions for each year.

NOTE J - EMPLOYEE HEALTH INSURANCE

The Medical Center is self-insured for health insurance claims of its employees. The Medical Center has reinsured a portion of its risk for such claims. The reinsurance arrangement covers annual claims in excess of \$75,000 for each covered individual. The reinsurance arrangement also covers aggregate annual claims in excess of an amount determined in relation to the number of individuals participating in the self-insured health benefits plan during the year. Covered employees also provide part of the funds to pay claims through monthly contributions at predetermined rates. Contributions by

SOUTHWEST MEDICAL CENTER
NOTES TO FINANCIAL STATEMENTS - CONTINUED
December 31, 2014 and 2013

NOTE J - EMPLOYEE HEALTH INSURANCE - Continued

the Medical Center and participating employees are remitted to the Southwest Medical Center Employee Health Plan Trust. The Trust has retained an insurance company as its agent to process and settle claims. The Trust reimburses the agent weekly for the amount of claims paid by the agent net of any amounts covered by reinsurance. The following is a summary of the activity under this arrangement:

	<u>2014</u>	<u>2013</u>
Estimated net health insurance claims payable at beginning of year	\$ 245,238	\$ 254,762
Provision for Medical Center's share of incurred claims and related expenses for the year, net of any reinsurance proceeds	1,906,742	1,507,579
Employee contributions	785,577	730,789
Payments made for claims and related expenses	<u>(2,692,265)</u>	<u>(2,247,892)</u>
Estimated net health insurance claims payable at end of year	245,292	245,238
Trust assets available for payment of claims and related expenses	<u>1,191,253</u>	<u>1,274,406</u>
Net estimated prepaid expense for health insurance claims at end of year	<u>\$ (945,961)</u>	<u>\$ (1,029,168)</u>

NOTE K - CONCENTRATION OF CREDIT RISK

The Medical Center grants credit without collateral to its patients, most of who are local residents and are insured under third-party payor agreements. The mix of receivables from patients and third-party payors at December 31, 2014 and 2013, is as follows:

	<u>2014</u>	<u>2013</u>
Medicare	16%	14%
Medicaid	12	13
Blue Cross	11	13
Other third-party payors	15	22
Self-pay	<u>46</u>	<u>38</u>
	<u>100%</u>	<u>100%</u>

SOUTHWEST MEDICAL CENTER
NOTES TO FINANCIAL STATEMENTS - CONTINUED
December 31, 2014 and 2013

NOTE L - RELATED PARTY TRANSACTIONS

During 2014 and 2013, the Medical Center received \$175,000 and \$100,000, respectively, from the Foundation for the purchase of property and equipment.

NOTE M - RISK MANAGEMENT

For the years ended December 31, 2014 and 2013, the Medical Center was insured for professional liability under a comprehensive hospital liability policy provided by an independent insurance carrier with limits of \$200,000 per occurrence up to an annual aggregate of \$600,000 for all claims made during the policy year. The Medical Center is further covered by the Kansas Health Care Stabilization Fund for claims in excess of its comprehensive hospital liability policy up to \$800,000 pursuant to any one judgment or settlement against the Medical Center for any one party, subject to an aggregate limitation for all judgments or settlements arising from all claims made in the policy year in the amount of \$2,400,000. The policy provided by the independent insurance carrier provides for umbrella liability coverage in excess of the underlying limits set forth above in the amount of \$2,000,000 per occurrence with an aggregate amount in any policy year of \$2,000,000. All coverage is on a claims-made basis. The above policies are currently in effect through November 21, 2015. The Medical Center intends to renew this coverage on that date and is aware of no reason why such coverage would be denied at that time.

In addition to the risks disclosed elsewhere in these financial statements and notes thereto, the Medical Center is exposed to various risks of loss related to torts; theft of, damage to, and destruction of assets; errors and omissions; injuries to employees; and natural disasters. The Medical Center purchases commercial insurance for these risks. Settled claims have not exceeded this commercial coverage in any of the past three years.

SUPPLEMENTARY INFORMATION

SOUTHWEST MEDICAL CENTER
BALANCE IN DEPOSITORY COMPARED WITH DEPOSITORY SECURITY
December 31, 2014

	<u>Bank balances</u>	<u>F.D.I.C. coverage</u>	<u>Balance subject to pledging of securities</u>	<u>Market value of securities pledged</u>	<u>Market value of securities pledged in excess of (less than) depository requirements</u>
First National Bank	\$ 12,527,500	\$ 250,000	\$ 12,277,500	\$ 13,496,610	\$ 1,219,110
Community Bank	6,000,000	250,000	5,750,000	5,786,919	36,919

SOUTHWEST MEDICAL CENTER
SCHEDULE OF REVENUES AND EXPENSES
WITH BUDGET COMPARISON
Year ended December 31, 2014

	<u>Actual</u>	<u>Budget</u>	Over <u>(under)</u>
Net patient service revenue	\$ 44,389,827	\$ 43,945,000	\$ 444,827
Other	<u>1,334,663</u>	<u>337,000</u>	<u>997,663</u>
Total operating revenues	45,724,490	44,282,000	1,442,490
Total operating expenses	<u>42,058,747</u>	<u>41,496,020</u>	<u>562,727</u>
Operating income	3,665,743	2,785,980	879,763
Nonoperating revenues (expenses)	<u>(670,480)</u>	<u>(507,000)</u>	<u>(163,480)</u>
Excess of revenues over expenses before capital grants and contributions	<u>\$ 2,995,263</u>	<u>\$ 2,278,980</u>	<u>\$ 716,283</u>

SOUTHWEST MEDICAL CENTER
SUMMARY OF INSURANCE COVERAGE

December 31, 2014

<u>Insurer</u>	<u>Type of coverage</u>	<u>Coverage amount</u>	<u>Term</u>
KaMMCO Insurance Company	Hospital professional liability Other liability Personal injury/property	HPL \$200,000/\$600,000 PL \$1,000,000/\$3,000,000 PIP \$1,000,000/\$1,000,000	November 21, 2014 to November 21, 2015
Kansas Health Care Provider Insurance Availability Act	Excess hospital professional liability	\$800,000/\$2,400,000	November 21, 2014 to November 21, 2015
KaMMCO Insurance Company	Umbrella liability	\$2,000,000/\$2,000,000	November 21, 2014 to November 21, 2015
Darwin Insurance Co.	Directors, Officers, and Trustees liability	\$2,000,000/\$2,000,000	November 21, 2014 to November 21, 2015
KaMMCO Insurance Company	Fire legal liability	\$50,000/\$50,000	November 21, 2014 to November 21, 2015
Travelers Insurance Company	Property	Real - \$55,240,800 Personal - \$24,898,200 Business interruption - \$31,631,868	June 30, 2014 to June 30, 2015
Hartford Insurance Company	Auto liability and physical damage	\$1,000,000/\$1,000,000	June 30, 2014 to June 30, 2015
Hartford Insurance Company	Commercial crime	Blanket employee dishonesty and forgery/alteration - \$100,000 Theft, burglary - \$10,000	June 30, 2014 to June 30, 2015
Travelers Insurance Company	Commercial crime	Excess employee dishonesty - \$250,000	June 30, 2014 to June 30, 2015
KHA Workers' Compensation Fund, Inc.	Workers' compensation and employers liability (Kansas)	Statutory: Bodily injury by accident - \$500,000 each accident Bodily injury by disease - \$500,000 policy limit Bodily injury by disease - \$500,000 each employee	January 1, 2014 to January 1, 2015